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U. S. CIRCUIT COURT OF APPEALS. FOURTH CIRCUIT

William J. Rahley, Def.-appellant) In
vs.) Equity
Columbia Phono. Co. , Comp.-appellee) No. 457

Appeal from the U.S. Circuit Ct. for the District of Maryland.

BRIEF FOR APPELLANT ---------

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FOURTH CIRCUIT.

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Appeal from the United States Circuit Court for the District of Maryland.

BRIEF FOR APPELLANT.

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U. S. Circuit Court of Appeals,

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WILLIAM J. RAHLEY, Appellant, vs. COLUMBIA PHONOGRAPH COMPANY, Appellee.	In Equity. No. 457.

APPEAL FROM THE U. S. CIRCUIT COURT FOR THE DISTRICT OF MARYLAND.

BRIEF FOR APPELLANT.

Statement of Facts.

On January 15th, 1889, the North American Phonograph Company, a New Jersey corporation, made an agreement with Edward D. Easton, constituting him the exclusive selling agent of phonographs and graphophones, and records and supplies therefor, for said company, in Maryland, Delaware and the District of Columbia for the period of five years from that date (Case, page 12). Phonographs and graphophones and the records and supplies used with them contain devices covered by patents of Thomas A. Edison and Bell & Tainter. The North American Phonograph Company never had any legal title to any of the patents of Mr. Edison relating to phonographs, records and supplies.

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(Case, page 63) This Easton agreement, while containing apparently important recitals, grants to Mr. Easton only selling rights. The important clauses in the agreement are the last sentence of paragraph first (Case, page 14) which is as follows :

" And the party of the first part will grant no other similar rights for this territory to others, or exercise any similar rights therein itself while this agreement remains in force."

And paragraph eighteen, upon which Judge MORRIS relies entirely in granting the preliminary injunction (Case, page 20) which is as follows :

" The party of the first part hereby agrees that, except as hereinafter otherwise provided, it will not during the continuance of this agreement, either directly or indirectly, through agents or otherwise, deal in any machines, instruments, contrivances or appliances of any kind or description within the territory covered by this agreement, except through the party of the second part or upon his written consent."

On June 13, 1889, an agreement was made between the North American Phonograph Company and the Columbia Phonograph Company, the complainant below, by which the Columbia Phonograph Company succeeded to Easton's rights, and the term of the first agreement was to be extended for ten additional years on the performance of certain conditions. (Case, page 6.) The provisions for the extension of the term are in paragraphs third and fourth of this second agreement. (Case, pages 9 and 10.) There is no proof in the case that those conditions precedent ever were fulfilled.

The North American Phonograph Company became insolvent and a Receiver for it was appointed in August, 1894. The said Receiver sold the assets of the corporation and some of them were purchased by the National Phonograph Company, which assets so purchased did not include any rights of the North American Phonograph Company under the said contracts with Easton and the Columbia Phonograph Company. (Case, pages 40 and

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41). The National Phonograph Company is not the successor of the North American Phonograph Company, and did not assume any of its obligations. (Case, page 40)

The National Phonograph Company received licenses from the Edison Phonograph Company and the American Graphophone Company, which said two companies own respectively the Edison and the Bell & Tainter Patents, which patents cover certain devices contained in phonographs and the records and supplies used with them. (Case, pages 42 to 45) The Columbia Phonograph Company is owned and controlled by the American Graphophone Company, and is its exclusive selling agent. Edward D. Easton, with whom the exclusive selling agency contract was made, is the president of both companies. (Case, pages 6 and 43) The Columbia Phonograph Company sells only graphophones. (Case, page 38)

The contract between the Columbia Phonograph Company and the North American Phonograph Company, on which this suit is brought, provides that the Columbia Phonograph Company shall offer both phonographs and graphophones to the public without discrimination. That clause in the contract is the second, and is as follows : (Case, page 14)

"The instrument which has been heretofore known or designated as the "graphophone," shall at all times and in all dealings, advertisements, agreements, business, &c., of the party of the second part be known, designated and described as the "phonograph-graphophone," and the instrument heretofore known or designated as the "phonograph" shall continue to be so known, designated and described. In dealing with the public and sub-lessees, the party of the second part shall and will at all times offer and show both instruments together with absolute impartiality, leaving the person or persons with whom he is dealing to make his or their own selection, and the party of the second part, his agents and employees shall in no way press the introduction of one instrument at the expense of the other, and the commissions or remuneration to agents, if any shall be employed, shall be the same on each instrument."

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The National Phonograph Company is engaged in selling phonographs, records and supplies under the said licenses from the Edison Phonograph Company and the American Graphophone Company. They are manufactured for it by the Edison Phonograph Works. Graphophones are manufactured by the American Graphophone Company, and the two machines are sold in competition with each other. (Case, page 38) Records can be used interchangeably on the two rival machines. The Columbia Phonograph Company has from time to time purchased from the National Phonograph Company parts of phonographs. (Case, pages 41, 46-62) These parts were sold in the regular way of business, and not under the Easton contract. (Case, page 41) The Easton contract provided for a special method by which such goods should be sold. It is found in Clause 11 of the contract (Case, page 17) which is as follows:

"If on the 1st day of January, 1890, or at any time thereafter the results of exclusively leasing instruments shall be satisfactory to the party of the first part, it may require the party of the second part to give the public the option of either leasing or purchasing the said instruments, and in such event sales shall be made at prices which shall be fixed by the party of the first part; provided, however, that if such requirement shall be made in the case of any one sub-company or agent, it shall be operative in the case of all sub-companies or agents acting under authority of The North American Phonograph Company, party of the first part, or Jesse H. Lippincott, sole licensee of the American Graphophone Company. From the price received for any instrument so sold there shall be first deducted and paid to the party of the first part an amount which shall be equal the actual cost of said instrument to the party of the first part, and the balance of said selling price shall be equally divided between the party of the first part and the party of the second part, settlements and payments to be made by the party of the second part on or before the 10th day of each month for all sales made during the previous month."

The National Phonograph Company sold to the defendant, who has a store in Baltimore, some phono-

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graphs, records and supplies. These sales were made at Orange, New Jersey. (Case, pp. 37, 39 and 40) The sales were "outright", but the defendant agreed not to sell the goods at less than certain prices and not to certain prescribed dealers. (Case, page 37) The defendant is not an agent of the National Phonograph Company. (Case, pages 37 and 40) Phonographs have been sold from time to time by other dealers in Baltimore. (Case, page 38) The defendant proceeded to sell these phonographs, records and supplies in Baltimore, and this bill was filed in the U. S. Circuit Court for the District of Maryland to restrain him from making further sales, and a preliminary injunction to that effect was granted; from the order granting which injunction this appeal is taken.

Phonographs and graphophones are machines similar in essential respects. They each consist of a tapering mandrel revolved by a motor, upon which the blank or the record can be placed, and a recorder or reproducer arranged to move longitudinally relative to the mandrel. The "blank" is a hollow cylinder of wax-like material. A recorder is a diaphragm in a suitable support having attached to it a cutting point. To make a "record," a "blank" is placed on the mandrel and the recorder put into operative relation with it. The motor is then started. Sound waves are impelled against the diaphragm and the cutting point cuts a helical groove in the surface of the "blank," in the bottom of which groove are formed elevations and depressions corresponding to the sound waves. This turns the "blank" into a "record." The reproducer is a diaphragm, having attached to it a blunt point. If one of these "records" is placed on the mandrel and the reproducer put into operative relation with it and the motor started, the sounds formerly recorded are audibly reproduced. These "records" are a commercial article sold in large quantities to the public generally.

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Assignment of Errors.

The Court below, in granting the preliminary injunction, erred in the following particulars.

1. It adjudged that the National Phonograph Company is the successor of the North American Phonograph Company, and is bound by its contracts; while the proofs show that the only relation between the two companies is that the National Phonograph Company purchased at Receiver's sale some of the assets of the North American Phonograph Company.

2. It adjudged that a patented article legally purchased from the patentee in one State may not be used or sold by the purchaser in other States, if the patentee has granted exclusive rights for its use and sale in such other States.

3. It adjudged that the freedom of transfer of chattels, thereafter to come into existence, may be restricted, as against a third party, by a contract not conferring any title to, or lien upon such chattles.

4. It adjudged that the covenant of the North American Phonograph Company not to sell phonographs in Maryland would prevent a perron lawfully purchasing phonographs from that company elsewhere, from selling them in Maryland.

5. It adjudged that the Easton contract has been extended beyond the first term of five years.

6. It adjudged that the Easton contract did not terminate with the insolvency and winding up of the North American Phonograph Company.

7. It adjudged that a party to a contract who is intentionally violating it, may still enforce it in equity against a third party, defendant, claiming under the other party to the contract.

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8. It adjudged that the license from the American Graphophone Company to the National Phonograph Company did not give a purchaser of phonographs from the latter company a right to use and sell them in Maryland.

9. It adjudged that the dealings between the Columbia Phonograph Company and the National Phonograph Company were not a conclusive admission that the Easton agreement was not in force as between those two companies.

10. It adjudged that a preliminary injunction should issue, although the rights of the complainant are doubtful and have never been established by any final decree in equity or judgment at law.

ARGUMENT.

I.

Patented articles lawfully sold in any portion of the United States may be legally used or sold anywhere within the United States.

Adams vs. Burke, 84 U. S., 453.

In this case it was held that a purchaser of a patented article from one territorial licensee may lawfully use it in the territory of another territorial licensee.

Hobbie vs. Jennison, 149 U. S., 355.

In this case it was decided that one territorial licensee who sold the patented articles in his own territory with the intention that they should be used

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in the territory of another territorial licensee, was not subject to suit by the territorial licensee.

Keeler vs. Standard Folding Bed Co., 157 U. S., 659.

In this case it was decided that:

"A dealer in patented articles doing business in Massachusetts, and knowing that the right to manufacture, use and sell such articles within that State belongs to another, may purchase such articles from the patentee in Michigan in the ordinary course of trade for the purpose of resale in Massachusetts, and may sell them there in defiance of the rights of the licensee."

II.

Freedom of use or sale of chattels, except under the Patent Laws, cannot be restricted; especially as to chattels to come into existence in the future, and by negative covenants.

The only covenant under which any restriction as to the sale or use of phonographs and records can be found is Section 18 of the contract between Edward D. Easton and the North American Phonograph Company, which is found on page 20 of the printed case, and is quoted at length on page of this brief. It is nothing more than a personal agreement on the part of the North American Phonograph Company not to sell the articles in question, either directly or indirectly, within the territory covered by the agreement, except through the Columbia Phonograph Company. There is no agreement that the chattels thereafter to be manufactured for, and sold by, the North American Phonograph Company, or leased by it should not be sold anywhere. The better considered cases hold that any contract forbidding the free sale and use of chattels is

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invalid against a third party even with notice, as imposing a restriction on the use and sale of chattels not recognized by law.

It is one of the elemental propositions of law that property can have imposed upon it only such incidents and restrictions as the law has from time immemorial recognized. The policy of the law is against restricting the sale or transfer of property, and especially of chattels. It is to the interest of the public that such sale and transfer should be as free and unrestricted as possible.

The following cases and citations from text books sustain these propositions, and the case of *Apollinaris Co. vs. Scheerer*, 27 F. R., 18, decided by that distinguished jurist, Judge WALLACE, of New York, is directly in point.

Apollinaris Co. vs. Scherer, 27 Fed. Rep., 18.

One Saxlehner owned the Hunyadi Janos Spring in Hungary and sold to the complainant the sole right to import and sell the waters of the spring in America. All the bottles sold in Europe containing the water had on them a label stating that they were not sold for export. The defendant bought bottles of the water in Europe and sold them in the United States with notice of the rights of the complainant. The complainant asked for an injunction, which was denied. Judge WALLACE in his opinion says:

"It was not possible by any contract or grant between Saxlehner and the complainant to create a territorial title to the products of the spring; no such title is known to the law of personal property. * * * The rights of the complainant rest purely in covenant. If Saxlehner himself should sell the water here the purchaser would acquire title to the article with all the rights of a proprietor to use it or do with it as he might see fit. Suppose the purchaser should be fully aware at the time of buying that Saxlehner had covenanted with the complainant that the latter alone should have the privilege of selling the water here, could it be seriously questioned that the purchaser would, nevertheless, acquire a perfect title? Although the defendant was fully aware, when he bought the water

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which he has imported from those to whom Saxlehner had sold it, of the terms of the agreement between Saxlehner and the complainant, that circumstance does not help the complainant's case. * * * The insuperable difficulty in the way of the complainant is that any purchaser of the water, wherever he purchases it, acquires a valid title to treat it as his own property."

Garst vs. Hall & Lyon Co., 179 Mass., 588.

A stipulation in a contract for the sale of a proprietary medicine, sold under a registered trade-mark, that the purchaser shall not sell it for less than a specified price, does not follow the medicine into the hands of a subsequent vendee, and he cannot be prevented at the suit of the manufacturer from selling at less than the stipulated price, although he knows that the manufacturer sells only subject to such stipulation.

See notes to same case reported 55 L. R. A., 630.

Brewer vs. Marshall, 19 N. J. Eq,, 537, 545.

The owner of land having on it a marl pit, sold it with a restrictive covenant that no marl should be sold from off the land. This covenant was not enforced against a subsequent purchaser of the land with notice upon the ground, among others, that a vender cannot impress upon land "any of his notions" not recognized by law.

Dwight on Personal Property, page 440.

"Without freedom of sale or exchange, ownership is not complete. Many movable articles are produced in great excess of the wants of the producer. To deny the right of sale would be to make the article comparatively valueless, and to check and embarrass production. In case of sale, the unrestricted right to make a succeeding sale passes to a purchaser. *If one should attempt to restrict a subsequent transfer, the restriction would be inoperative and void.*"

The only cases bearing on this proposition which might be considered as contravening the above, are:

New York Bank Note Co. vs. Hamilton Bank Note Engraving and Printing Co., 83 Hun, 593; 31 N. Y. Supp., 1060.

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New York Bank Note Co. vs. Hamilton Bank Note Engraving and Printing Co., 28 App. Div., 411; 50 N. Y. Supp., 1093.

We maintain that these cases are not good law and should not be followed by the courts of other States. But if they are good law, they are not applicable to this case. They hold merely that a covenant in regard to an *existing* chattel restricting its use can be enforced against a subsequent purchaser, with notice.

The unwisdom of a recognition by the Courts of the legality of such a contract is evident at once. It would enable a corporation, or an individual, to impose upon any chattel thereafter sold by the corporation or the individual a restriction as to its use, which, if proper notice of the restriction were placed on the chattel, would last so long as the judicial system of this country lasts. Under the patent laws Congress has restricted monopolies to seventeen years. All other legal monopolies are restricted in time. Why then, therefore, should it be within the power of individuals to create quasi-monopolies so entirely foreign to the spirit of the common law?

III.

The National Phonograph Company never became in any way bound by the contracts entered into by the North American Phonograph Company.

Judge MORRIS in his decision entirely overlooked the proofs before him. The complainant's bill of complaint alleges upon information and belief "that the National Phonograph Company, named as a defendant herein, is successor in the phonograph business of the said North American Phonograph Company, and is bound

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by the contracts and agreement of the latter." There is absolutely no proof to support this allegation. On the contrary, the affidavit of William E. Gilmore, who is the president of the National Phonograph Company and is familiar with all the details of its affairs, states that the only relation between the two companies is that the National Phonograph Company purchased at the Receiver's sale certain assets of the North American Phonograph Company. He states (case, p. 40):

"The National Phonograph Company is not the successor in business of the North American Phonograph Company. It has not assumed the obligations of any of the contracts of the North American Phonograph Company."

And on page 41:

"The National Phonograph Company purchased some of the said remaining assets of the North American Phonograph Company, but did not purchase any rights of the North American Phonograph Company in the contracts made by that company with Edward D. Easton and the Columbia Phonograph Company."

No attempt has been made to contradict this conclusive proof, although his affidavit was filed on April 16th, 1901, and the complainant was allowed to file a rebutting affidavit on May 13th, 1901.

The taking over by one corporation of the entire assets, franchises and business of another would not cause the former to become bound by the contracts of the latter in the absence of an express agreement to that effect.

Houston, etc., R. R. Co. vs. Shirley, 54 Texas, 125.
Powell vs. N. Missouri R. R. Co., 42 Mo., 63.
Sappington vs. Little Rock, &c., R. R. Co., 37 Ark., 23.
Traction Co. vs. Offutt, 17 App. Cas., D. of C., 292, 308:

"Nor can we see how, in the absence of legal provision, a company which purchases the property and franchises of another company, can, by virtue of such

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purchase, be charged with the liabilities of the company from which it purchased."

Where the property and franchises of a railroad company have been sold under a mortgage and a new company organized, the new company is not liable for the debts of the old.

Smith vs. Chicago & N. W. R. R. Co., 18 Wis., 1.

"The result of a transaction of this kind is to form a new corporation to carry on the business of the old company upon a new basis, free from its debts and obligations, except to the extent that they have been expressly assumed."

Morawetz on Private Corporations, 2d Ed., § 812.
Lake Erie, &c., Co. vs. Griffin, 92 Ind., 487.
Pennsylvania Transportation Co.'s Appeal, 101 Pa. St., 576.
Menasha vs. Milwaukee, &c., R. R. Co., 52 Wis., 414, 420.

This rule is, of course, not applicable where property is purchased to which some third party has some title—*e. g.*, a license under a patent. In such a case a purchaser with notice takes subject to the outstanding title. But that is not the present case in any respect, although the Court of Appeals of the District of Columbia fell into that error. It erroneously assumed that the "North American Phonograph Company * * * at the time had full and complete control over the Edison phonograph patents."

Even if the title to the Edison Patents were in the North American Phonograph Company, it would not avail the complainant here. If the complainant seeks to found its case on that title, it should have framed its bill under the United States Patent Laws and not as an ordinary bill in equity to restrain the violation of a contract.

The title of the North American Phonograph Company to the Edison phonograph patents is discussed at length under Point IV. of this brief.

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The question as to whether the National Phonograph Company is bound by the contracts of the North American Phonograph Company is absolutely vital on this appeal. There is really no pretense on the part of the complainant below that it has any rights in this matter, unless the National Phongraph Company is bound by these contracts; and Judge MORRIS bases his decision entirely on the assumption that the National Phonograph Company is so bound. That portion of his opinion begins at the last paragraph of page 154 of the printed case, and ends at the beginning of the last paragraph of page 155. It is only necessary to read that to see upon what he bases his opinion and the error into which he fell.

While the appellant does not admit that even if the National Phonograph Company was bound by the contract of the North American Phonograph Company, he, the appellant, could be restrained from using and selling in this territory, chattels lawfully purchased from the National Phonograph Company, even with knowledge of the contract, we confidently submit that the complainant's case must fall on account of there being no proof to connect the National Phonograph Company with the contracts of the North American Company.

IV.

The North American Phonograph Company never had any title to the Edison Phonograph Patents.

The evidence *pro* and *con* adduced in the case is brief. The complainant's bill, paragraph 1, alleges in effect that by virtue of four certain agreements, identified by their dates, the entire title and ownership of certain phonograph patents of Mr. Edison vested in the North American Phonograph Company. (Case, page

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2) The contents of the agreements are not set forth; so these allegations of the bill, although sworn to, are merely conclusions of law. These agreements were not produced at the hearing, although proffered by the complainant and demanded by the defendant. (Case, page 39)

The complainant's president, Edward D. Easton, swears that at the time of the organization of the Columbia Phonograph Company the North American Phonograph Company was "the owner of the phonograph patents and inventions of Thomas A. Edison." (Case, page 24) He does not give the source of his information and does not state that the North American Phonograph Company owned the patents when it made with him the contract of Jauuary 15, 1889, upon which this suit is based.

The defendant swears, on information and belief, that the North American Phonograph Company never acquired any title to any letters patent of the United States granted on inventions of Thomas A. Edison. (Case, pages 38 and 39)

Cassell Severance swears that he has examined the records of the Patent Office and finds that none of the phonograph patents of Thomas A. Edison have ever been assigned to the North American Phonograph Company so far as those records show. (Case, pages 63–65) This is, of course, not positive proof, as assignments may have been made and not recorded. But the custom is so general to record assigunents of patents that it is strong presumptive proof.

Mr. Mauro, the complainant's counsel, in the first paragraph of his affidavit (Case, pages 143 and 144) gives an account of the condition of the title to the Edison phonograph patents on August 1, 1888, materially differing from the allegations of the bill and from Mr. Easton's affidavit. He presents copies of two of the agreements referred to in paragraph 1 of the bill of complaint. His affidavit must be read in conjunction with the agreements and is proof only so far as the

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Court's construction of the agreements bears out Mr. Mauro's conclusions.

The first contract he produces is between Thomas A. Edison and Jesse H. Lippincott, dated June 28, 1888. (Case, pages 148-150) It recites that the Edison phonograph patents issued up to that time are owned by the Edison Phonograph Company, and that Mr. Edison owns a majority of the stock of the company. Mr. Edison then agrees to sell said stock to Lippincott for $500,000. Mr. Mauro further deposes that Lippincott conveyed to the North American Phonograph Company all his rights in the Edison Patents. There is absolutely no legal proof of this last allegation.

He further testifies that this supposed conveyance by Lippincott to the North American Phonograph Company was confirmed by Mr. Edison by the agreement of August 1, 1888, a copy which he produces. That agreement recites that the North American Phonograph Company "has acquired the necessary rights and authority" to exploit and introduce commercially the phonograph. (Case, p. 145) As to just what that right and authority consist of, we are left in the dark. Paragraph fourth of the agreement provides that any invention or improvement made on the phonograph by Mr. Edison within fifteen years from the date of the agreement (August 1, 1888) should be assigned to the North American Phonograph Company. (Case, p. 146)

The proven facts, therefore, are that the Edison Phonograph Company owns all the Edison phonograph patents issued prior to June 28, 1888, which includes all those mentioned in the Easton contract of January 15, 1889 ; (see Caswell Severance's Affidavit, Case, pp. 63–65) that the North American Phonograph Company did not become the owner of a majority of the stock of the Edison Phonograph Company ; and that Mr. Edison was under agreement to assign to the North American Phonograph Company all inventions and improvements on the phonograph made by him within fifteen years from August 1, 1888.

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This last agreement of Mr. Edison did not give the North American Phonograph Company such an interest in any patents issued for such inventions as entitled it to sue infringers, or as enabled it to grant to others such licenses as would entitle the licensee to maintain such a suit.

Dueber vs. Fahys, 45 Fed. Rep., 697 (Syllabus):

"A suit for infringement of letters patent cannot be maintained, where it appears that the complainant has not the legal title to any of the patents, but has merely the defendant's contract to convey them."

All that the North American Phonograph Company could have done, if Mr. Edison refused to assign the patents, was to file a bill in equity against him for specific performance, or to bring a suit at law for damages.

Regan, &c., Co. vs. Pacific, &c., Co., 49 Fed. Rep., 68:

"A contract by which A does 'license, grant and convey' any invention he may thereafter make in gas engines to B, does not operate as an assignment of such invention when made, and, at most, gives to A the right in equity to have an assignment of such invention to him."

It is doubtful, however, whether even this relief would be granted.

Kennedy vs. Hazelton, 128 U. S., 667:

"Specific performance cannot be decreed of an agreement to convey property which has no existence, or to which the defendant has no title; and if the want of title was known to the plaintiff at the time of beginning the suit, the bill will not be retained for assessment of damages.

"One who agrees to assign to another any patent that he may obtain for improvements in certain machines and who afterwards invents such an improvement, and, with intent to evade his agreement and to defraud the other party, procures a patent for his invention to be obtained upon the application of a third person, and to be issued to him as assignee of that person, and to receive profits under it, cannot be

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compelled in equity to assign the patent or to account for the profits."

There is, however, another paragraph in this contract to be considered. It is the ninth. (Case, page 147) It provides that upon the failure of Lippincott to pay Edison the $500,000 provided in the contract of June 28, 1888, "this contract shall be null and void." Howard W. Hayes swears in his affidavit (Case, page 151) that this $500,000 "was never fully paid by said Jesse H. Lippincott." Mr. Hayes states that he is familiar with the facts in question, and gives the source of his familiarity. In the absence of contradiction, his affidavit must be taken as true and the contract of August 1, 1888, considered as "null and void."

Mr. Hayes also states specifically that "the North American Phonograph Company never became the owner of said [Edison Phonograph Company] stock, or any part thereof, or ever had possession of it, and never held or exercised any ownership over any Edison phonograph Patent." In view of Mr. Hayes' full acquaintance with all the facts, these statements must be taken as more than counterbalancing the allegations of the bill and Mr. Easton's and Mr. Mauro's affidavits.

Even if the North American Phonograph Company had become the owner of a majority or all of the stock of the Edison Phonograph Company, it would not have owned the assets of that corporation and could have granted no rights under the patents belonging to it.

Porter vs. Pittsburgh Bessemer Steel Co., 120 U. S., 649, 670:

"The mere fact that Crawford owned a majority of the stock did not give him the legal control of the company."

Pullman Car Co. vs. Mo. Pac. Railroad Co., 115 U. S., 587 (at p. 597):

"The Missouri Pacific Company has bought the stock of the St. Louis, Iron Mountain & Southern Company, and has effected a satisfactory election of

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directors, but this is all. It has all the advantages of a control of the road, but that is not, in law, the control itself. Practically it may control the company, but the company alone controls its road. In a sense the stockholders of a corporation own its property, but they are not the managers of its business, or in the immediate control of its affairs. Ordinarily they elect the governing body of the corporation, and that body controls its property. Such is the case here. The Missouri Pacific Company owns enough of the stock of the St. Louis, Iron Mountain & Southern to control the election of directors, and this it has done. The directors now control the road through their own agents and executive officers, and these agents and officers are in no way under the direction of the Missouri Pacific Company. If they or the directors act contrary to the wishes of the Missouri Pacific Company, that company has no power to prevent it, except by the election at the proper time and in the proper way, of other directors, or by some judicial proceeding for the protection of its interests as a stockholder. *Its rights and its powers are those of a stockholder only. It is not the corporation, in the sense of that term as applied to the management of the corporate business or the control of the corporate property.*"

Jessup vs. Illinois Cent. R. R., 36 F. R., 735 (syllabus):

"An averment in the bill that defendant has obtained control of the stock of the D. Co. does not show that the two companies have become merged into one, but simply that defendant has obtained a majority of the stock of the D. Co."

Exchange Bank vs. Macon, 97 Ga., 1 (syllabus):

"The fact that one corporation owns the entire capital stock of another, does not vest in the former the legal title to the property of the latter."

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V.

The rights of the complainant under the contract with the North American Phonograph Company terminated on the death of that company, and then became merely a claim for damages.

Construing the contract most favorably to the complainant, it will be found that it recites that the North American Phonograph Company owns *or* controls *or* has a right to use certain letters patent of Mr. Edison and the inventions covered thereby, and that Mr. Easton desired to obtain such exclusive rights under lease and license from the North American Phonograph Company. Notwithstanding these recitals there are no grants or words of grant in the contract, nor any grant of any right whatever under these patents or for these inventions. It merely provides, in the fourth section, that the North American Phonograph Company will lease to Mr. Easton phonographs which Mr. Easton may sublet in the District of Columbia and the States of Maryland and Delaware, and in the eleventh, that under certain circumstances the North American Phonograph Company may require Mr. Easton to give to the public the option of purchasing phonographs ; in which case they shall be sold at a price to be fixed by the North American Phonograph Company, with a fixed arrangement for division of profits.

The only covenants on the part of the North American Phonograph Company, upon which any rights claimed by Easton can be founded, are that the North American Phonograph Company will grant no other similar rights for this territory to others, nor exercise any other similar rights therein itself while the agreement remains in force. That is found in the first section. And that the North American Phonograph Company will not deal in any machines, instruments, contrivances or appliances within the territory covered

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by the agreement. This covenant is found in section eighteen, and repeated verbatim in the twenty-second section.

It is evident that this contract is merely one of an exclusive selling agency, a species of contract very commonly entered into by corporations with agents in different territories. Such a contract does not give the agent any right to prevent another party from selling or using the articles in such territory. And on the insolvency and dissolution of a corporation the selling agency terminates and becomes a claim for damages. Upon the winding up of the North American Phonograph Company the Columbia Phonograph Company could have, as did other similar selling agency companies, presented a claim for damages to the Receiver. The North American Phonograph Company while it lived was a New Jersey corporation. The contract between the parties was made in New Jersey and must be construed according to the laws of New Jersey, which is the *lex loci contractus*. The decisions in that State are unanimous in so construing such a contract.

Spader vs. Mural Decoration Co., 47 N. J. Eq., 18.

Rosenbaum vs. U. S. Credit System Co., 61 N. J. Law, 543.

VI.

The rights under the Easton contract, whatever they were, terminated five years from its date; as it was never extended.

The contract with Mr. Easton provided in section first, on page 14 of the printed case, that it should continue "until the 15th day of January, A. D. 1894, or for such further period as hereinafter provided."

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Section 19, on pages 20 and 21 of the printed case, provides for an extension of the agreement until the 26th day of March, 1903, upon the deposit of 5,000 shares of its capital stock in a trust company for the benefit of the North American Phonograph Company, and the delivery of the stock at the expiration of the said five years to the North American Phonograph Company, or to Jesse H. Lippincott, trustee. By a subsequent agreement made on June 13th, 1889, found on pages 6 to 11 of the printed case, it is recited that the stock of the said company had been deposited with a trust company, as required by the former agreement. And it further provides in sections 3 and 4 of the said contract, found on page 9 of the printed case, that the trust company is to deliver said stock on January 15, 1894, to Jesse H. Lippincott, trustee, and that upon such delivery the said agreement shall be extended to March 26, 1903.

That delivery, as a matter of fact, never took place; and the complainant does not claim any such delivery in its moving papers, nor does it allege any excuse for such non-delivery. Without such delivery, or a legal excuse for the failure to deliver, the complainant, by its own papers, proves itself out of court.

VII.

The Columbia Phonograph Company, in its dealings with the National Phonograph Company conclusively admitted that the contract with Easton, under which it now claims these imaginary rights, is not in force.

The affidavit of William E. Gilmore (Case, page 41) and the correspondence between the two companies

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and bills of sale annexed to his affidavit (Case, pages 46-62) show that the Columbia Phonograph Company dealt with the National Phonograph Company merely as a purchaser, in the same manner as the National Phonograph Company has always dealt with the defendant and many other dealers in Baltimore and other portions of the alleged exclusive territory of the complainant.

This correspondence shows that negotiations were carried on in regard to the prices of goods, what discounts should be allowed, and the like. The contract in question provides specifically that goods are either to be leased to Easton to be sub-let to the public or, at the option of the North American Phonograph Company, are to be sold to the public at a price to be fixed by the North American Phonograph Company, from which price is to be deducted first the cost of manufacture and then the balance is to be divided equally between the North American Phonograph Company and the complainant. (Section eleventh; Case, page 17) If the complainant or the National Phonograph Company had considered that agreement as being in force, no such negotiations as shown would have been carried on between them, nor such sales made. Evidently neither party ever considered the agreement as having survived the death of the North American Phonograph Company, or as in any way binding on the National Phonograph Company.

The continued breaches by the complainant of essential provisions of the contract, set out fully in Point IX., also show that it no longer considered the contract in force. The Columbia Phonograph Company is in the position of either deliberately violating its contract or of having honestly considered it as no longer in force. Where a situation like this is open to two constructions, one consistent with honest dealings and the other not, the Court will, if possible, adopt the former. But, at any rate, the complainant is in the dilemma of having to admit that the contract is not in force since the winding up of the North American

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Phonograph Company, or of coming into a court of equity without clean hands.

This latter branch of this last proposition is discussed in Point IX.

VIII.

The National Phonograph Company received from the American Graphophone Company a licence which is in effect a right to make, use and sell the devices in question, in the territory claimed by the complainant.

The complainant is the sole selling agent of the American Graphophone Company. The advertising circulars of the complainant offered in evidence in the court below admit this. The president of the complainant is Edward D. Easton, as appears from Mr. Easton's affidavit found on page 6 of the printed case. He is the same Edward D. Easton with whom the North American Phonograph Company entered into the contract of January 15th, 1899, upon which this suit is based. Mr. Easton is also the president of the American Graphophone Company, and signed the license above referred to on behalf of the American Graphophone Company. It is found on pages 42 and 43 of the printed case.

This American Graphophone Company is the real complainant in this case, and the license to the National Phonograph Company, under the patents owned by the American Graphophone Company, carries with it, beyond question, a right to use and sell phonographs in any portion of the United States, including this territory, an exclusive right in which is claimed by the Columbia Phonograph Company the sole selling agent and *alter ego* of the American Graphophone Company.

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It is a gross abuse of the process of a court of equity for the American Graphophone Company with one hand and for a valuable consideration, to give to the National Phonograph Company a license to make, use and sell phonographs, and with the other, through its selling agent the Columbia Phonograph Company, to attempt to deprive the National Phonograph Company and its purchaser of that right in this manner; a purchaser from the National Phonograph Company, as this appellant is, necessarily acquires all the rights to use and sell machines that its vendor had.

IX.

The complainant below is not entitled to any relief in a court of equity, as it conclusively appears that it has deliberately broken, to the injury of the defendant's vendor, important provisions of the contract upon which it bases its alleged right to the extraordinary relief asked for.

The Columbia Phonograph Company is the *alter ego* of the American Graphophone Company. Edward D. Easton is the president of both companies, and the Columbia Phonograph Company sells exclusively the talking machine called the "graphophone," manufactured by the American Graphophone Company, which is inferior to the Edison phonograph but is sold in competition with it.

The Columbia Phonograph Company, the complainant, does not and has not sold the phonograph, but devotes all its energies to placing the graphophone on the market. Its advertising literature, copies of which appear in the case, show every effort to push the sale of the graphophone, under the name "graphophone"

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and not "phonograph-graphophone," and without a mention of the phonograph. The business conduct of the complainant shows where its interest lies and shows the purpose of this suit.

Yet the contract, under which the complainant claims its imaginary rights, specifically provides, in section two, that the complainant shall present to the public both the phonograph and the graphophone with absolute impartiality, leaving the public to select which one they wish, and also provides that the graphophone shall always be known as the "phonograph-graphophone". The purpose of these requirements on the part of the North American Phonograph Company is obvious. That company wished to protect itself against just such actions on the part of the complainant as has appeared in this case; and the complainant, having deliberately and continually violated one of the most essential requirements of the contract under which it claims its alleged rights, is not in a position to come into a court of equity and ask that any successor of the North American Phonograph Company, or any vendee from such successor, shall be prevented from offering and selling to the public the phonographs which the complainant under its contract was bound to offer to the public, and which it has refused so to do in order that it might advance the business of its principal, the American Graphophone Company, at the expense of the companies manufacturing and selling the phonograph. Surely there could not be a clearer case where the doctrine must be enforced, that he who comes into equity must come with clean hands.

"He who seeks the aid of equity to enjoin the violation of an agreement, or for the protection of his contract rights, must himself come into court with clean hands; and to entitle himself to relief he must have carried out as far as possible his own part of the contract."

High on Injunctions, Vol. 2, page 733, Sec. 1119.
Stiff vs. Cassell, 2 Jur. N. S., 348.
Fechter vs. Montgomery, 33 Beav., 22.

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"If the complainant refuses to fulfil any of his obligations in matters of substance under the license, a court of equity will not interfere to assist him in compelling the defendant to observe the obligations upon his part."

Foster vs. Goldschmidt, 21 Fed. Rep. 70. (Syllabus.)

In discussing this point, I have spoken as if the North American Phonograph Company was still in existence and had itself, in violation of its contract, sold phonographs and supplies in the District of Columbia; and I have put the argument in that form (which is the strongest possible form for the complainant) in order to show how absolutely without equity the complainant stands.

X.

Where there is any doubt as to the complainant's rights, a preliminary injunction will not issue.

It is unnecessary to quote decisions in support of this well-established principle, but I will refer to the following cases:

Home Ins. Co. vs. Nobles, 63 F., 642.
Paine vs. U. S. Playing Card Co., 90 F., 543.
American Preservers' Co. vs. Norris, 43 F., 711.
Mowry vs. Railroad Co., 5 Fisher 587.

The only suggestion that can be made by the appellee in answer to this is, that at times a court of equity will issue a preliminary injunction to maintain the *status quo*. But in this case there is no *status quo* to be preserved. The complainant below is not engaged in the business of selling phonographs or phonograph supplies, and therefore cannot be injured by the sale of

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phonographs by other parties. On the other hand, a preliminary injunction works a great hardship on the defendant. In his affidavit on page 160 of the printed case, he says :

" My business of selling phonographs and phonograph supplies is small, but taken into conjunction with my other business, enables me to pay my expenses and allows me a small profit. Without this part of my business I would not be able to meet my expenses; paying rent, clerk hire, etc., or continue in business. It would be a great hardship on me if I am restrained from selling phonographs or supplies while this suit is still pending."

And on page 38 of the printed case he says that when the agent of the complainant called on him he urged him to deal in graphophones instead of phonographs, and on his refusal so to do threatened him with this suit.

XI.

The Court below was misled as to the effect of decisions appearing to have some bearing on this case.

None of these decisions, except that of the Court of Appeals of the District of Columbia, has any bearing on this case whatever. The decisions are as follows :

Columbia Phonograph Co. vs. North American Phonograph Co., Tewkesbury and Spencer (Sup. Ct. D. of C., 1893; not reported).

This was a bill filed under the United States patent laws for an infringement of the Edison patents described in the Easton contract. That it was considered purely a patent bill and not one, like the bill in this case, to enforce contract rights, appears from the prayer of the bill; (Case, page 76) the opinion of Judge Cox,

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(Case, page 26) and the decree for injunction, (Case, page 102). The answers (Case, pages 92 and 100) did not dispute the title to the patents, their validity or the infringement. The defense set up was that the machines had been lawfully purchased from a territorial licensee and so could be used anywhere. Judge Cox overruled this defense and attempted to distinguish Adams vs. Burke, 84 U. S., 453; but that question has been set at rest by Keeler vs. Standard Bed Co., 157 U. S., 659. Judge Cox's decision, therefore, can have no weight now.

New England Phonograph Co. vs. Edison et al., 110 Fed. Rep., 26:

This case came up on a demurrer to a bill of complaint and the Court did nothing more than say that the learned counsel who prepared the bill was able to state a case which he should be allowed to prove in court. The bill is not against a dealer like the present appellant, but against the National Phonograph Company and others, and its principal allegation is a conspiracy on the part of the defendants to defraud the plaintiff of its rights under a contract. The contract itself was not considered by the Court, not being before it, and Judge GRAY passes only upon the allegations in the bill. The bill alleges "a sole and exclusive grant to the complainant of the right to use, and sell phonographs within the territory named." It also alleges that the defendants were bound by the contracts of the North American Phonograph Company, and alleges that the defendants themselves, although bound by those contracts, proceeded to violate them. Judge GRAY decided that these allegations made out a good ground of action. But it will be seen at once that that opinion has no bearing on this case, as it did not decide that a purchaser from a company bound by such a contract was also bound by it, and did not pass upon the question as to whether the National Phonograph Company was in any way bound by the contracts of the North American Phonograph Company. It also appears, from the recital of the contract in the bill of complaint, that

it is quite different from the present contract, as the contract referred to in that bill of complaint granted exclusive rights to use and sell phonographs and appliances within the New England States, and did not contain merely the negative covenant set out in paragraph 18 of the contract produced in the present case, upon which covenant the opinion below is entirely based.

New York Phonograph Co. vs. National Phonograph Co., 112 Fed. Rep., 822:

In this case Judge WHEELER does nothing more than follow the opinion of Judge GRAY, and to say that, without the allegations of conspiracy, a good case would be made out against the National Phonograph Company if it could be shown that the complainant was an exclusive licensee for the use and sub-letting of phonographs in the State of New York, and that the defendant was so connected with the licensor as to be bound by the terms of the license and had violated the covenant implied from the exclusiveness of the license. It will be seen at once that this opinion passes on nothing more than was passed upon by Judge GRAY, and does not meet the two important elements in this case—viz., as to whether a third party purchasing a chattel under the circumstances appearing in this case can be restrained from selling it in the territory claimed by the complainant, nor as to whether the National Phonograph Company is in any way connected with, or bound by, the contracts of the North American Phonograph Company. No covenant contained in either of the contracts involved in those cases (which contracts are dissimilar from the contracts in the present case) were passed upon as to their legal effect.

Columbia Phonograph Co. vs. Whitson, Court of Appeals, District of Columbia, April term, 1901:

It is true that in this case the Court passed upon the same contract involved in this case. But the ground upon which the opinion was based is not tenable, and in no way supports Judge MORRIS's decision. Further-

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more, the Court based its decision on facts not proven in this case.

We would call the Court's attention to many details of the opinion. After reciting facts alleged in the plaintiff's bills and affidavits, and the defendant's affidavits, the opinion refers to the provision in the Federal statute for assigning patent rights, and goes on to state that the "North American Phonograph Company, which at the time had full and complete control over the Edison phonograph patents," granted to the plaintiff an exclusive territorial right to deal in phonographs.

"Any person natural or artificial, into whose hands, after the execution of the contract between the North American Phonograph Company and the Columbia Phonograph Company, the control of the Edison patents came, with knowledge or notice, actual or constructive of the existence of said contracts and of the rights of the Columbia Phonograph Company must be assumed to have taken subject to such rights, and be disqualified from infringing in any manner the exclusive license given to the Columbia Company. If that were not so it is very plain that rights granted under a patent might be destroyed with impunity against the will of the owner by mere transfer of the patent."

From the foregoing it is evident that the Court of Appeals considered that the plaintiff in that case had brought suit against the defendant under the patent laws of the United States to restrain the defendant from infringing patents under which the plaintiff had an exclusive territorial license. Assuming those facts to exist, there would be, of course, no question as to the correctness of the above quoted legal proposition. And assuming, as we must, that the facts in that case were such as found by the Court of Appeals, that case may have been correctly decided; but it has no bearing whatever on this case, which is not brought for infringement of a patent; in which it is not shown that the licensor had any title to the patents in question; or that the licensee received any license under any patents; or that the instruments sold and used by the defendant contained any devices covered by the claims of any patent.

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The Court of Appeals further says:

"It is understood that the deposit of stock required to be made by the Columbia Phonograph Company was duly made, and that the extension of its exclusive right and privilege under the contract thereupon became effective until March 23, 1903."

Whatever might have been the proof in that case, that fact does not appear in this case. The contract here presented provides that the extension should not become effective until the stock was delivered to Lippincott and the contract delivered to the Columbia Company. There is no proof that this was ever done. On the contrary, it is denied.

The Court further says:

"The contract between the North American Company and the Columbia Company may be defective and insufficient, but it would scarcely be proper so to hold at this hearing, when the real parties in interest might not be bound by the decision and the cause has not been fully developed by testimony."

Yet this contract, which "*may be defective and insufficient,*" is the only basis for the complainant's claim in this case. It is the complainant's sole muniment of title. If there is any question as to the plaintiff's title, a preliminary injunction should not be granted.

We, therefore, submit that the opinion of the Court below finds no support, either as to its law or its facts as applicable to this case, in the decision of any other court.

We submit that, in view of the disputed questions of fact; in view of the more than doubtful validity of the complainant's alleged rights; in view of the lack of any injury to the complainant, and in view of the great injury done by the preliminary injunction to the defendant, the decree granting it should be reversed.

HARDCASTLE & WYNN,
Solicitors and of Counsel of Appellant.

HOWARD W. HAYES,
Of Counsel.

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